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States Oppose IRS Plan to Loosen Privacy Rules on Taxpayers' Returns

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Attorneys General from 46 states and Washington D.C have filed formal objections to proposed Internal Revenue Service (IRS) rules that would increase taxpayers' exposure to identity theft by making it easier for businesses to share and use personal information included on tax returns.

"In the guise of increasing taxpayers' control over their return information, the IRS wants to move in exactly the opposite direction," said California Attorney General Bill Lockyer. "This proposal is more than misguided. It's dangerous. By eroding the security of private information, the regulations would increase consumers' exposure to identity theft and invasive, unlawful marketing practices."

The objections were bipartisan, with Lockyer, a Democrat, and Washington Attorney General Rob McKenna, a Republican, the co-sponsors. Lockyer wrote the comments.

"We are greatly concerned that **this regulation** *(http://www.consumeraffairs.com//news04/2006/03/irs_data_sales.html)*, if adopted as proposed, will erode consumer privacy and the security of sensitive personal information, with a consequent increase in such serious problems as identity theft and intrusive or even abusive marketing practices," the Attorneys General wrote.

They expressed agreement with the IRS's stated goal to enhance taxpayers' control over the use of their return information, but added, "We are troubled, however, by the provisions of the proposed regulations that seem to undermine rather than advance that goal."

The AGs said "the best, most prudent course" the IRS could take to protect individuals' privacy would be to ban tax preparers from sharing their customers' information for any purpose unrelated to preparation of tax returns. The top state prosecutors pointedly noted consumers are not clamoring to make their personal financial information more available to more businesses.

"There is simply too much at risk for American taxpayers ... to increase the likelihood that their most personal information will be stolen or misused," the Attorneys General wrote. "Crucially, there is no pressing need to put that information at risk: American consumers' financial information is already copiously provided to businesses offering financial services and related products. We are aware of no complaints from taxpayers that they receive too few solicitations from these companies."

Tax preparers covered by IRS regulations include accountants and other individuals, as well as tax preparation firms. Current IRS rules allow tax preparers, after obtaining customers' written consent, to share return information with banks and other third parties to facilitate offering of ancillary, tax-related services.

Such services include "refund anticipation loans (RALs)," high-interest loans sold to taxpayers based on their projected refund. Earlier this year, filed a lawsuit against **H&R Block** *(http://www.consumeraffairs.com/finance/hr_block_ral.html)*, charging that the firm violated 15 separate state and federal laws in marketing and selling RALs. Among the laws Block allegedly violated are federal and state rules that prohibit unauthorized sharing and use of personal information on taxpayers' returns.

Despite these problems, the IRS' proposed regulations would expand preparers' ability to share taxpayers' personal information, and third parties' ability to access and use that information.

Specifically, the rules would allow preparers, with written consent, to share or sell customers' return information with any third party, including third parties that have no arrangements with the tax preparer to provide ancillary, tax-related services. Not bound by the regulations, the third parties then could use the information for marketing or other purposes without obtaining consumers' consent.

Unrelated third parties could include data brokers such as **ChoicePoint** *(http://www.consumeraffairs.com/news04/2005/choicepoint.html)*, which unwittingly sold large numbers of individuals' private information to identity thieves. Some critics have argued the regulations could position tax preparers as data brokers themselves, selling taxpayers' personal financial information for substantial profit.

If the IRS does not prohibit tax preparers from sharing customers' return information for marketing purposes, the Attorneys General recommended the agency adopt specific measures to significantly reduce the practice and strengthen privacy protections.

For example, the Attorneys General said the rules should mandate that preparers, before sharing return information for use in providing RALs and other ancillary services, first obtain third parties' agreement to not use the information for any other purpose.

Additionally, the AGs recommended the regulations include disclosure requirements to ensure taxpayers give separate, knowing and voluntary consent to each specific use of their return information.

The IRS also should prohibit tax preparers from conditioning the provision of any service on taxpayers' agreeing to share their return information, the Attorneys General said. They noted they have "encountered ... instances in which a tax preparer has required taxpayers to consent to disclose their personal information to marketers of IRAs as a condition for being considered for a refund anticipation loan."

To further safeguard privacy, tax preparers should be prohibited from using or disclosing return information not needed to obtain the specific services requested by customers, the Attorneys General recommended.

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